

## 30 Second M&A Newsletter

### How will rising interest rates affect M&A?

There's zero doubt that interest rates are going up this year. The Fed issued a 0.25 percentage point rate hike in March, the first increase we've seen since late 2018, and a second in June of 0.75. But more increases are coming in the year ahead.

In normal times, as interest rates go up, the value of businesses come down. When interest rates climb, buyers have to pay more for the underlying business loan. Because their debt now costs more, they need to pay less for their acquisition in order to get the same rate of return on their dollars.

We haven't seen price adjustments yet with the first rate hikes, but we may start to see that happening further in the year as additional increases occur.

What's interesting is that these aren't exactly normal times. Private equity activity is still blazing hot. These firms raised over \$900 billion in capital last year and invested a record \$1 trillion for the first time. There's so much money chasing deals, it may take a while for valuations to cool off.

One camp says investors will lower their expectations for returns. We're seeing that playing out in private equity. Speaking with one private equity firm, they use to project a 22% rate of return for their investors. Now they believe their limited partners will be happy with 15% - 20% returns – results still better than investors can get in just about any asset class.

Another camp believes valuations will be negatively affected. It's all in the numbers. If interest rates are higher, then financing costs are higher and the amount a buyer can pay goes down. Likewise, rising interest rates can have a dampening effect on general economic confidence. We see a downtick in the stock market; it has a carryover effect on the M&A market.

But for now, the M&A market doesn't appear to be running out of steam. Some dealmakers believe we'll break last year's records. Interest rates are still low (for now), lending is aggressive, and private equity continues record fundraising. All in all, that means we're seeing the hallmarks of a robust period for M&A.

Are there headwinds ahead? Rising inflation and global tensions could limit how much further this cycle will continue. Some economists are projecting a recession in 2024. Will M&A hold out that long? Dealmakers will be watching to see how the market responds.



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